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SUBJECT: TURKEY STEAM ENERGY CONFERENCE IN ISTANBUL - LIBERALIZATION AND REGIONAL CHALLENGES AND OPPORTUNITIES

REF: A. ANKARA 6195

1B. ANKARA 6479

11. (SBU) SUMMARY: A well-attended energy conference in Turkey provided expressions of commitment on the part of the government to move forward on energy liberalization, but failure to articulate next policy, legislative, and regulatory steps. The private sector is eager to move ahead and take advantage of potential investment opportunities, but is frustrated that the liberalization process and timing remain unclear. Conflict between the Energy Ministry and the Energy Market Regulatory Authority (EMRA) contribute to the lack of clarity. Because of long lead times for energy project finance and construction, Turkey may face a shortage of electric power generation capacity in 3-5 years if it fails to foster a positive investment environment now. END SUMMARY.

12. (SBU) Embassy Energy Officer David Young and Economic Specialist Aysem Sargin attended the fourth STEAM (Strategic and Technical Economic Research Center) sponsored "Energy Arena" in Istanbul November 23-24. STEAM has established itself as one of the premier sponsors of energy sector conferences in Turkey and the session was well attended by high-level officials from the GOT (Energy Minister, Undersecretary, Dep U/S, MFA, TPAO, etc.) and the private sector (Shell, BP, Chevron-Texaco, etc.) Overall, government officials expressed commitment to energy liberalization, while private sector reps expressed strong interest, but frustration with continued questions on timing and process. Regional issues, including East-West Corridor and Iraq linkages were major topics.

Electricity

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13. (SBU) The biggest domestic issues on participants' minds were the prospective liberalization and privatization of Turkey's electric and natural gas distribution networks. While Turkish officials stressed their commitment to move forward (Budak Dilli, DG Energy Affairs, MENR, was particularly impassioned on the topic), private sector players were frustrated by the many delays and lack of clarity. Despite twenty municipal distribution networks for electricity distribution having been identified, there have still been legal and regulatory delays. The World Bank electricity liberalization road map was viewed as very helpful, but again implementation has been delayed because of gaps in legal and regulatory underpinning. Many licenses have been granted for electricity production, but, here too, there have been delays in implementation. There was great interest from the private sector in possible privatization of EUAS (the state electricity production company), but still questions on process and timing. (The most likely approach would be bundling of small, regional groups of diverse energy type facilities.)

Natural Gas ) Volumes Not Contracts Transfer?

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14. (SBU) In his speech, Energy Minister Guler emphasized increased interest in renewables and nuclear (he recently announced a desire to put in place multiple power plants), as well as the recent tenders for transfer of BOTAS natural gas take or pay purchase contracts to private companies (septel). Although there are press reports of significant interest, private comments indicated skepticism on whether the tenders will succeed and questions about the exact rules and process.

In effect, the current tender is for the "right to negotiate" with BOTAS' purchase contract sales partners (i.e., Russia) without knowing confidential existing contract terms. Many observers expect legal obstacles may force Turkey to opt later to selling gas volumes via tenders, rather than the underlying gas contracts. Public expression of interest may be jockeying for the presumed next step of transfer of gas volumes. There were also concerns expressed in the corridor about Bosphorus Gas having insider knowledge or position in the tender process because of significant ownership from Gazprom (forty percent).

Russia Connection

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15. (SBU) BP officials also privately expressed concerns that some expiring Russian contracts might be extended, potentially putting at risk the procurement of Shah Deniz gas from Azerbaijan. Separately, the GOT has tendered nineteen contracts for municipal natural gas distribution. Russian entities have indicated interest in these. (Note: There will be incentives for GOT and GOR to find energy deliverables in advance of President Putin visit December 5-6. End Note) Although, the natural gas distribution privatization process is still underway; many contacts felt pre-qualification procedures have not been sufficient, so it is unclear if early winners can achieve their commitments. (Note: The World Bank and GOT released a natural gas sector strategy paper in September, citing domestic liberalization as critical from a number of perspectives, including realization of regional transit opportunities.)

Electricity Export to Iraq  
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16. (SBU) Many discussions moved beyond domestic liberalization to regional issues. Energy Undersecretary Demirbilek privately blamed EMRA (Energy Market Regulatory Authority) for the Karadeniz Company's problems in exporting electricity to northern Iraq, including excessive costs for purchases of electricity off the grid (Ref A). (Note: There was general and frequent "bashing" of EMRA at the conference. End Note.) Karadeniz was the main conference sponsor, which earned them a seat on a panel to describe their challenges in implementing their "power for friendship" program with Iraq.

Bosphorus Bypass  
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17. (SBU) MFA DDG for Energy Hakkı Akil used the conference as a platform to articulate the Bosphorus bypass dilemma and the value of "Voluntary Principles" as a constructive public/private approach for encouraging transit of oil through pipelines "as long as it is commercially feasible", as an alternative to shipping through the Turkish Straits. While Akil applauded the new VTS (Vessel Transit System) as a great addition for safety, he emphasized the importance of working together to realize oil bypass pipeline solutions. As an example of a country limiting tanker traffic for safety reasons, he pointed out that Italy has forbidden passage of oil tankers between Sardinia and the mainland. Akil rearticulated support for Samsun-Ceyhan as the best bypass option, given existing infrastructure and environmental concerns about trans-Thrace proposals. There were some private comments in support of the Voluntary Principles, but also questions about next steps (who actually signs? how to engage Russians?). On another topic, Akil noted that in order to avoid succumbing to the pressure of connecting to the large gas reserves in Iran, there should be collective efforts to link with Turkmenistan.

18. (SBU) In BP rep Mike Bilbo's public comments, he stressed the environmental standards set by BTC, noting the intense NGO pressure which had come to bear on the project. Citing Alaska, he noted that using pipelines over tankers was becoming a more accepted solution for moving large quantities of crude oil to markets. With respect to BTC, he noted that there was no room to relax, now that construction was nearly complete; the project would be operational fifty plus years and would require consistent diplomatic efforts.

19. (SBU) In an opening speech and CNN Turk interview, Ankara Energy Officer Young stressed the consistency of U.S. regional energy policy, strong support for liberalization and contract sanctity and a Bosphorus bypass (but we don't pick the winner; GOT should move forward on awarding timely permits to let investors take on the risk), and strong U.S. opposition to links to Iran. Apart from an "agreement to disagree" on policy with respect to Iran, there was broad acceptance of U.S. regional energy policy and recognition of the value of the U.S. as an actor in moving the East-West Energy Corridor forward.

10. (SBU) Comment: Although interested in liberalization and privatization opportunities, companies are skeptical and frustrated about delays in filling in the blanks of the new regulatory and legal structure for the energy sector. Lack of clarity resulting in further delays in liberalization is a clear disincentive to new investment. This could put Turkey at risk in 3-5 years when the GOT and most observers estimate that there will be a shortage of electricity generation supply in Turkey. End Comment.

11. (U) Baghdad minimize considered. EDELMAN